

## Message Text

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ACTION ARA-15

INFO OCT-01 ISO-00 SOE-02 AID-05 CEA-01 CIAE-00  
COME-00 DODE-00 EB-08 DOE-15 H-01 INR-10 INT-05  
L-03 NSAE-00 NSC-05 OMB-01 PM-05 ICA-11 OES-09  
SP-02 SS-15 STR-07 TRSE-00 ACDA-12 PA-01 XMB-02  
/136 W

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P 082137Z SEP 78

FM AMEMBASSY MEXICO

TO SECSTATE WASHDC PRIORITY 2541

C O N F I D E N T I A L SECTION 01 OF 02 MEXICO 14783

E.O. 11652: N/A

TAGS:ENRG, MX

SUBJECT: NATURAL GAS TALKS

REF: MEXICO 12476

SUMMARY. PRESIDENT LOPEZ POTRILLO'S INFORME (PERTINENT PASSAGES QUOTED IN PARA 7 BELOW) CRITICIZED THE US FOR REFUSING TO OFFER "FAIR VALUE" FOR MEXICO'S GAS, BUT CLEARLY LEFT THE DOOR OPEN FOR EVENTUAL GAS SALES TO THE US. WHILE NO INITIATIVE WITH THE MEXICANS IS CALLED FOR IMMEDIATELY, THE US SHOULD BE CONSIDERING HOW IT WILL APPROACH THE BASIC AREAS OF DISAGREEMENT WHEN NEGOTIATIONS ARE RESUMED. ACTION REQUESTED: DEPT.'S VIEWS REQUESTED ON SUGGESTIONS CONTAINED IN PARA 5 BELOW. END SUMMARY.

1. PRESIDENT LOPEZ PORTILLO'S INFORME CLEARLY DID NOT ELIMINATE THE POSSIBILITY OF FUTURE GAS SALES TO THE US. I AM HOPEFUL THAT FAVORABLE ACTION ON THE CONFERENCE COMMITTEE REPORT WILL PERMIT US TO APPROACH LOPEZ PORTILLO AND FIND A WAY TO RESUME NEGOTIATIONS.

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2. IT MIGHT BE USEFUL THEN TO SUGGEST TO LOPEZ PORTILLO THAT THE USG WOULD CONSIDER A COMPROMISE ON THE QUESTION OF PRICE ESCALATION, WHICH APPEARS TO BE THE MAIN IMPEDIMENT TO AGREEMENT. I HAVE IN MIND THE COMPROMISE DRAWN UP BETWEEN THE PACIFIC LIGHTING CORP. AND INDONESIA, I.E., 50 PERCENT LINK TO WORLD OIL PRICES (WITH A 15 PERCENT CEILING) AND A 50 PERCENT LINK TO THE US WHOLESALE PRICE

INDEX. I UNDERSTAND THAT THIS COMPROMISE IS BEING SERIOUSLY CONSIDERED.

3. THIS CONCEPT, ADJUSTED AS NECESSARY FOR THE MEXICAN CASE, WOULD SEEM TO MEET THE USG REQUIREMENT FOR A KNOWN AND REASONABLE ESCALATOR AND THE MEXICAN DESIRE FOR A LINK TO WORLD OIL PRICES.

4. IN ADDITION, I HAVE BEEN APPROACHED BY GABRIEL ALARCON, PRESIDENT AND DIRECTOR GENERAL OF EL HERALDO (A GENERALLY CONSERVATIVE AND PRO-AMERICAN PAPER), WITH THE SUGGESTION THAT THE US CONSIDER AN ADVANCE PAYMENT FOR MEXICAN GAS SIMILAR TO THE RECENT JAPANESE PREPURCHASE OF URANIUM FUEL. ALARCON HAS ALSO APPROACHED LOPEZ PORTILLO WITH THIS IDEA AND, WHILE THE USG IS NOT INVOLVED IN THE ACTUAL PURCHASE OF GAS, WE CAN APPROACH THE CONSORTIUM MEMBERS TO SEE IF THEY ARE WILLING TO MAKE SUCH A PAYMENT OR ARRANGE FINANCING. THE COMPANIES INDICATED THAT THEY MIGHT BE WILLING TO DO SOMETHING ALONG THESE LINES WHEN THE WORLD BANK LOAN LIMITATIONS APPEARED TO BE A PROBLEM. THE MEXICANS MIGHT FIND ADVANCE PAYMENT, AT LEAST SUFFICIENT TO PAY FOR THE SAN FERNANDO-REYNOSA LINE, VERY APPEALING.

5. I THINK IT WOULD BE USEFUL TO APPROACH LOPEZ PORTILLO WITH A PACKAGE FOR HIS CONSIDERATION CONSISTING OF THE FOLLOWING FOUR ELEMENTS: THE COMPROMISE DESCRIBED IN CONFIDENTIAL

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PARAS 2 AND 3; THE ADVANCE PAYMENT CONCEPT IN PARA 4 (DEPENDING OF COURSE ON THE CONSORTIUM MEMBERS' WILLINGNESS TO MAKE SUCH AN OFFER); AN ASSURANCE THAT THE CURRENTLY HELD-UP EXIM PIPELINE CREDITS WILL BE AVAILABLE AS SOON AS A CONTRACT IS APPROVED BY THE USG REGULATORY AGENCIES (AND PERHAPS AN ESTIMATE OF THE LENGTH OF TIME THAT PROCESS MAY REQUIRE); AND OUR PAPER DETAILING THE COSTS OF INCREASED MEXICAN DOMESTIC GAS USE (REFTEL).

6. I WOULD BE INTERESTED IN THE DEPARTMENT'S VIEWS ON THE ELEMENTS OF THIS APPROACH AND ON THE USEFULNESS OF PRESENTING SUCH A PACKAGE TO LOPEZ PORTILLO.

7. THE FOLLOWING ARE PASSAGES FROM THE OFFICIAL ENGLISH TRANSLATION OF PRESIDENT LOPEZ PORTILLO'S INFORME THAT DEALT DIRECTLY WITH NATURAL GAS.  
BEGIN TEXT.

OVER A YEAR AGO, WE HAD TO CHOOSE BETWEEN MASSIVELY EXPORTING OIL-ASSOCIATED GAS, CONSUMING IT DOMESTICALLY, OR BURNING IT. WE CHOSE TO EXPORT IT, BECAUSE THIS WOULD BRING US CONSIDERABLE AMOUNTS OF FOREIGN CURRENCY MORE QUICKLY, THUS ALLOWING US TO SOLVE OUR STILL OVER-

WHELMING PROBLEMS...

THE OTHER ALTERNATIVE, TO USE THE GAS IN MEXICO,  
REQUIRED MORE TIME, MORE PROMOTION, AND WOULD GENERATE  
LESS FOREIGN CURRENCY IN THE SHORT TERM.

THIS IS WHY, ASSUMING A TRADITIONALLY STRUCTURED FREE  
MARKET, PRELIMINARY AGREEMENTS WERE REACHED WITH FOREIGN  
COMPANIES...

ONE FORGETS THAT GAS HAS FUEL VALUE EQUIVALENT TO THAT  
OF OTHER COMBUSTION FUELS.

LOGICALLY, IT SHOULD BE WORTH MORE, BUT THIS IS NOT THE  
CASE WITHIN THE PRESENT STRUCTURE OF TRANSACTIONS AND  
WASTE. OUR POSITION, HOWEVER, REMAINS THE SAME: WE  
MUST GIVE GAS ITS REAL VALUE.

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IF WE HAVE A SURPLUS, WE CAN SELL, CONSUME OR KEEP IT  
IN RESERVE; BUT WE WILL NEVER UNDERSSELL IT, WHICH WOULD

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ACTION ARA-15

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SP-02 SS-15 STR-07 TRSE-00 ACDA-12 PA-01 XMB-02  
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P 082137Z SEP 78

FM AMEMBASSY MEXICO

TO SECSTATE WASHDC PRIORITY 2542

C O N F I D E N T I A L SECTION 02 OF 02 MEXICO 14783

BE EQUIVALENT TO BURNING IT.

WE DID NOT WANT TO INTERVENE IN THE DOMESTIC PROBLEMS  
OF OTHER COUNTRIES, WHICH ARE IN THE PROCESS OF DEFIN-  
ING THEIR ENERGY POLICIES. WHEN THE TIME LIMIT RAN

OUT, WE SIMPLY WITHDREW FROM THE AGREEMENT AND FELL BACK ON THE OTHER ALTERNATIVE: CONSUMING OUR GAS HERE, IN ORDER TO SUBSTITUTE IT FOR OTHER FUELS OR INPUTS AND THUS MAKE OPTIMUM USE OF OUR HYDROCARBONS. THE CONSTRUCTION OF THE GAS PIPELINE IS ON SCHEDULE AND IS COSTING MUCH LESS, IN TERMS OF INVESTMENT, THAN THE FIRST PROJECT WOULD HAVE. WE HAVE PRACTICALLY ENSURED THE USE OF THE SOUTHEAST'S ENTIRE GAS PRODUCTION, AND CAN AT OUR CONVENIENCE CHOOSE WHETHER OR NOT TO EXTRACT THE GAS IN THE NORTH AND TO CONSTRUCT PRIORITY INFRA-STRUCTURE WORKS FOR THE STIMULATION OF INDUSTRIALIZATION PROGRAMS IN SUITABLE ZONES...

OUR POTENTIAL AND OUR GEOGRAPHIC LOCATION ARE SUCH THAT OUR POSITION AS REGARDS FOSSIL FUELS CAN REPRESENT A PRESSURE OF WORLDWIDE SIGNIFICANCE. THEREFORE, WE ONCE AGAIN REAFFIRM MEXICO'S LINE OF CONDUCT. WE HAVE MAINTAINED OUR UNSHAKEABLE DESIRE TO GIVE RAW MATERIALS

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THEIR TRUE VALUE. NEITHER NOW NOR IN THE FUTURE WILL WE SABOTAGE THE EFFORTS OF THOSE WHO, LIKE OURSELVES, ARE FIGHTING FOR THIS. IT IS A FUNDAMENTAL PART OF THE NEW INTERNATIONAL ECONOMIC ORDER WE ARE FIGHTING TO OBTAIN. THAT IS WHY WE HAVE SOLD OUR CRUDE OIL AT TOP PRICES ON THE INTERNATIONAL MARKET; THAT IS WHY WE DID NOT SELL OUR GAS. WE KNOW THAT LOW PRICES KEEP THE NEW OIL-PRODUCING REGIONS OF THE WORLD FROM PROSPERING AND GROWING. END TEXT. LUCEY

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